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RUCPDO/DEPT OF COMMERCE WASHINGTON DC  
RUEATRS/DEPT OF TREASURY WASHINGTON DC  
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UNCLAS SECTION 01 OF 02 SHANGHAI 000581

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USDOC FOR ITA DAS KASOFF, MELCHER, MAC/OCEA  
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SUBJECT: ECONOMIC CRISIS CRIMPING REVENUES OF ZHEJIANG EXPORT HUB

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¶1. (SBU) Summary: Slowing economic activity in Ningbo, a major port in Zhejiang Province, is leading to much lower revenue growth, which in turn will impact Central Government finances, according to the chief economist of the local planning commission. Ningbo's growth is on a declining trend, and the economist predicts it will decline to a 10 percent annual rate in 2009; especially worrying is slowing export growth. Enterprises are facing liquidity problems as bank loans and foreign investment become scarce, so Ningbo is planning a stimulus program that could consume a large proportion of local revenues, said the economist. End summary.

¶2. (U) Ningbo has the second largest GDP among cities in Zhejiang Province, accounting for approximately 18 percent of the total. Ningbo's GDP in 2007 was RMB343.3 billion (currently equivalent to US\$50 billion) and grew at an annual rate of 14.8 percent; in the first half of 2008 it grew at an 11.4 percent rate. The Port of Ningbo, a natural deepwater port and one of China's oldest ports, now handles approximately 7 percent of China's total trade volume. Ningbo is China's second biggest port in tonnage and fourth largest in containers. In 2007, Ningbo's exports grew 33 percent and imports grew 35.7 percent.

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Lower Revenue Growth in Ningbo . . .  
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¶3. (SBU) Slowing economic activity in Ningbo is leading to much lower revenue growth, Ningbo Municipal Development and Reform Commission Chief Economist Zhan Rongsheng told Econoff on December 10, 2008. Ningbo government revenues generally grow 20 percent annually, said Zhan, but through October this year, growth fell to 15-16 percent; the year end figure will probably reach only 15 percent.

¶4. (SBU) Ningbo's overall economic growth is on a declining trend, said Zhan. He predicts that GDP growth will fall to 10 percent in 2009, with a slower first half and a rising second half. Zhan estimated that Ningbo's 2007 fiscal income was over RMB70 billion (currently equivalent to US\$10.21 billion), with additional off-budget income of RMB10 billion (US\$1.46 billion)

coming mostly from land transfers to property developers.  
(Note: Land sales are likely to stall as property developers trim back projects in the face of lower real estate demand. End note.)

¶5. (SBU) There are some worrying signs for exports, said Zhan, potentially putting further pressure on government revenues. Overall Ningbo exports grew 25 percent in the first 10 months over the same period last year, on particularly strong sales growth to new markets in the Middle East and Africa; however, exports to the United States fell 2 percent in the same period. (Note: In November, overall exports contracted by 1.1 percent, of which new and high technology product exports contracted 11.3 percent, according to the Ningbo Statistical Bureau. End note.)

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. . . Will Directly Impact Central Government Coffers  
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¶6. (SBU) Because Ningbo is a "city with subprovincial-level status" (fushengji chengshi), Ningbo's lower revenue growth will mean lower revenue income for the Central Government. Ningbo negotiates its contribution to state coffers with the Central Government, bypassing the provincial capital of Hangzhou, explained Zhan. In 2007, for instance, Ningbo handed over around 60 percent of on-budget revenues to the Central Government, he said.

¶7. (SBU) As part of its special status, Ningbo makes only a nominal contribution to provincial revenues, said Zhan. The municipality transfers a negotiated, fixed amount to the provincial capital of Hangzhou for use in poor areas of Zhejiang. Zhan estimated that this amount amounts to much less than 5 percent of the city's annual budget. However, Zhan said that Greater Ningbo is further divided into the city center, which has the subprovincial-level city status, and the outer

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counties, which are managed by the province. Taxes from the outer counties are part of the provincial budget.

¶8. (U) (Note: Nationwide in China there are 15 subprovincial level cities, mostly provincial capitals. Cities with this status that are not provincial capitals are Dalian, Ningbo, Qingdao, Shenzhen, and Xiamen. Zhan said that as part of its special status, top Ningbo officials are directly appointed by Communist Party Organization Department. In addition, Ningbo is a city specifically designated in the state plan (jihua danlie shi), said Zhan. This status gives Ningbo some independent economic planning authority. End note.)

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Corporate Finance Getting Pinched  
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¶9. (SBU) Banks are afraid to give loans and foreign investors are not increasing their local stakes, Zhan said, putting strains on corporate finance. Very few foreign invested companies in Ningbo are from the United States -- most are from Japan, Taiwan, and Hong Kong, explained Zhan. Of these, Taiwan and Hong Kong investors were simply maintaining their stakes (Zhan thereby implied that Japanese investors were drawing down their stakes). Overall, capital outflows are not large, said Zhan, since foreign-invested firms in Ningbo are still making money. (Comment: November's export contraction probably changes this picture. End comment.)

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Planning a Local Economic Stimulus  
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¶10. (SBU) Ningbo is planning a RMB80 billion (US\$11.67 billion) stimulus plan over the coming two years to combat the economic growth slowdown, said Zhan. About one-third of the capital will come from the Ningbo municipal budget. In addition, there will be investments by state-owned companies, bank loans (zhengfu

yinhang rongzi), and bank loans with local government guarantees (zhengfu juzhai). Zhan explained that the latter was basically local borrowing from banks, although the funds had to be approved and granted by the National Development Reform Commission. Ningbo authorities anticipate that the RMB80 billion will be matched by private capital of RMB300 billion (US\$43.78 billion), said Zhan.

¶11. (SBU) The RMB80 billion stimulus will be spent on 7 areas, said Zhan: 1) subsidized housing construction, 2) major infrastructure, 3) energy conservation and environmental protection projects, 4) improving people's living standards, 5) rural construction, 6) large-scale industrial projects, and 7) major urban public services.

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Comment  
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¶12. (SBU) Ningbo's finances are a microcosm of the opposing forces that will come into play in the export-oriented coastal provinces of the Shanghai Consular district in coming months. Booming urban areas that in the past have made disproportionate contributions to Central Government revenues will most likely argue that they need to retain a larger proportion of their tax intake to fund local economic stimulus plans. Already in Ningbo's case, the local government by Zhan's calculation currently retains only approximately RMB38 billion of its on- and off-budget income (RMB28 billion of taxes and RMB10 billion from land sales); as economic growth slows, however, these levels are likely to come under pressure. On the other hand, Ningbo is planning to kick around RMB26 billion of municipal funds over each of the next two years into the stimulus measures.  
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